Lim Yoke Kian & Anor v Castle Development Sdn Bhd

COURT OF APPEAL (KUALA LUMPUR) — CIVIL APPEAL NO W-02-747 OF 1996
NH CHAN, ABDUL MALEK AHMAD AND MOKHTAR SIDIN JJCA
19 JANUARY 1998

Companies and Corporations *— Winding up — Deferrement of winding up proceedings — Intention of shareholders to minimize payment of income tax — Whether amount to tax evasion — Whether illegality — Whether court should order winding up*

The petitioners sought a court order to wind up the first respondent on the ground that it had by special resolution resolved that it be wound up by the court. It was submitted that on the advice of their tax consultant, the shareholders of the first respondent decided to have their winding up deferred in order to minimize the payment of income tax. The petitioners argued that the court was condoning the tax evasion tactic of the first respondent if it chose to defer the winding up proceedings. The trial judge held that the court had discretion whether or not to order the winding up and dismissed the petition as he found that the decision to defer did not amount to tax evasion but an arrangement to attract the minimum liability to tax. The petitioners appealed.

Held, allowing the appeal:

It cannot be disputed that it was the intention of the shareholders to defer the winding up to minimize the payment of income tax, and this clearly was an illegality, not realizing that as the tax would be determined at the date of disposal, it really would not have make any difference as to when the winding up took place. Having considered the arguments and the authorities, the court was of the view that the learned trial judge was in error when he refused to order the winding up (see p 448A–B).

[Bahasa Malaysia summary

Pempetisyen memohon perintah mahkamah untuk menggulung responden pertama atas alasan bahawa ia telah melalui resolusi khas menetapkan bahawa ia hendaklah digulung oleh mahkamah. Dihujahkan bahawa atas nasihat perunding cukai mereka, pemegang-pemegang saham responden pertama berkeputusan untuk menundakan penggulungan mereka agar dapat mengurangkan pembayaran cukai pendapatan. Pempetisyen berhujah bahawa mahkamah membiarkan taktik responden pertama mengelakkan cukai jika ia memilih untuk menundakan prosiding penggulungan tersebut. Hakim perbicaraan memutuskan bahawa mahkamah mempunyai budi bicara sama ada untuk memerintahkan penggulungan tersebut atau pun tidak dan menolak petisyen tersebut

kerana beliau mendapati bahawa keputusan untuk menunda tidak bermaksud untuk mengelakkan cukai tetapi adalah suatu pengaturan untuk mendapatkan tanggungan yang minima untuk dicukai. Pempetisyen-pempetisyen tersebut telah merayu.

Diputuskan, membenarkan rayuan tersebut:

Tidak boleh dipertikaikan bahawa adalah merupakan niat pemegang-pemegang saham untuk menundakan penggulungan tersebut bagi mengurangkan pembayaran cukai pendapatan, dan ini jelas merupakan suatu kepenyalahan undang-undang, dengan tidak menyedari bahawa oleh kerana cukai akan ditentukan pada tarikh pelupusan, adalah sesungguhnya tiada apa-apa perbezaan berhubung dengan bilakah penggulungan tersebut berlaku. Setelah mempertimbangkan penghujahan-penghujahan dan autoriti-autoriti, mahkamah berpendapat bahawa hakim yang arif tersalah pertimbangan bila mana beliau enggan untuk memerintahkan penggulungan tersebut (lihat ms 448A–B).]

Notes

For cases on winding up generally, see 3 *Mallal's Digest* (4th Ed, 1997 Reissue) paras 618–918.

Cases referred to

Byrom Motors (Pvt) Ltd v Dolphin House (Pvt) Ltd [1958] 3 SALR 432 (refd)

Lai Kim Loi v Dato Lai Fook Kim & Anor [1989] 2 MLJ 290 (refd)

Lim Kar Bee v Duofortis Properties (M) Sdn Bhd [1992] 2 MLJ 281 (refd)

Legislation referred to

Companies Act 1965 ss 181, 218(1)(a), (i), 259(1)

Contracts Act 1950 s 24(b)

Appeal from: Company Winding Up No D4–28–9 of 1993

Raja Aziz Addruse (*Rita Phuah Lay Fong* and *Robyn Choi* with him) (*Lai Yoong Rita*) for the appellants.

Tommy Thomas (*Alex De Silva* with him) (*Skrine & Co*) for the respondent.

Abdul Malek Ahmad FCJ (delivering judgment of the court): The petitioners in the court below, who are the appellants before us, had sought a court order to wind up the first respondent, who is the only respondent in this appeal, on the grounds that it had by special resolution resolved that it be wound up by the court and that it was just and equitable that it be wound up under s 218(1)(a) and (i) respectively of the Companies Act 1965 ('the Act').

A At all material times, the shareholders of the first respondent were the second, third, fourth, fifth and sixth respondents. On 11 June 1991, the first respondent at an extraordinary general meeting passed a resolution approving the sale of Lots 2063 and 651 Mukim of Kuala Lumpur to Bolton Properties Bhd ('Bolton') for RM6,034,123. It was also resolved that approval be given for the purchase of 500,000 shares in Bolton together B with the bonus and rights entitlement from Kenneison Brothers Bhd for RM1,600,000.

It was the first petitioner's proposal that the first respondent be wound up after the sale of the land to enable the immediate distribution of the proceeds among the shareholders after the sale. At the extraordinary general C meeting on the 18 June 1991, approval was given for the said land to be sold to Bolton for RM5,500,000 and that the first respondent be wound up three months after the completion of the sale. Notwithstanding the resolution, the winding up did not take place and the petitioners are not happy that the directors of the first respondent are still conducting the company's affairs.

A number of preliminary objections were raised in court at the hearing D of the winding up petition by learned counsel for the second, fourth and seventh respondents. The first was that the petitioners were not members of the first respondent and were not pursuing relief under s 181 of the Act. This was conceded to by learned counsel for the petitioners.

The next preliminary objection was that this was a hybrid petition as E para 22 and 23 of the petition relate to s 181 of the Act whereas para 24 of the petition referred to s 218 of the Act.

The reply from learned counsel for the petitioners was that paras 22 and 23 are to be ignored but it was not wrong to bring in the second, fourth and seventh respondents as they were directors of the first respondent apart F from being shareholders against whom they had obtained a court order restraining them from holding an annual general meeting. Learned counsel for the said respondents immediately gave his undertaking that they would not convene any meeting pending the outcome of the petition.

The learned Judge ordered the petitioners to amend the petition relying on *Lai Kim Loi v Dato Lai Fook Kim & Anor* [1989] 2 MLJ 290 and the G matter was accordingly adjourned.

Learned counsel for the respondents at the continued hearing referred to para 11 of the affidavit of the seventh respondent filed on 18 August 1994 which stated that the board of directors of the first, respondent had been advised by their tax consultant that should the company be wound up, the H gain from the sale of the property from which real property gain tax of RM264,564 had been paid might subsequently be reviewed and reassessed as being an income from trading by the Department of Inland Revenue and with the imposition of this income and development tax and with the tax on the proceeds of the compulsory acquisition of part of the property in 1989 by the State Government, the additional tax would be in the region of I RM2,176,393. This would result in lower dividends for the shareholders of the first respondent upon winding up. In view of this, the board of directors of the first respondent felt it was best to prolong the period before the voluntary winding up proposed by the special resolution on 18 June 1991.

It was the argument of learned counsel for the petitioners that the court was condoning the tax evasion tactic of the first respondent if it chose to defer the winding up proceedings against the first respondent. A

The learned trial judge dealt with this issue in the following manner:

> The court has the discretion whether to order the winding up of a company by a special resolution. The word in s 218(1)(a) is 'may'. In England the same word is used. In *Byrom Motors (Pvt) Ltd v Dolphin House (Pvt) Ltd* [1958] 3 SALR 432, Quenet J said at p 534: B
>
> > 'Section 173 (a) of the Companies Act, 47 of 1951, provides that a company may be wound (sic) up by the court if the company by special resolution resolved that It should be wound up by the court ... I cannot with respect agree with the view that the court has no discretion in the C matter. Section 259(1) requires the court to have regard to the proved wishes of the creditors and contributories in all matters relating to a winding up.'
>
> The question here is whether or not the court should make a winding up order or not. Mr Thomas said that members of the Lim's family owned 60% of the shares and they had the right to get the best return from their capital. D Shareholders can do what they want with their shares: *Pender v Lushington* (1877) 6 Ch 70.
>
> In this case Castle is entitled to manage Its affairs 'so that the tax attaching under the appropriate acts is less than (sic) it otherwise would be'. *Comptroller of Income Tax v AB Estates Ltd* [1950–1985] MSTC 95 at p 96. E Acting on the advice (sic) of the consultant the directors decided to differ (sic) the voluntary winding. I disagree with Miss Rita Phua that what they were doing amounted to tax evasion or tax avoidance. What the directors were doing was to arrange the affairs of the (sic) Castle in such a manner as to attract the minimum liability to tax: *Chua Lip Kong v Director-General of Inland Revenue* [1982] 1 MLJ 235.
>
> For the reasons stated above, I dismiss the petition with costs. F

Before us, the short submissions of learned counsel for the appellants was that the petition was pursuant to a special resolution passed by all shareholders on 18 June 1991 to have the assets disposed of to be followed by the winding up three months later and that all payments had been made and there was no impediment to the winding up. G

However, on the advice of their tax consultant, it was decided by the shareholders of the first respondent who hold the majority shares to have the winding up deferred in order to minimize the payment of income tax. It was the contention of learned counsel for the appellants that as tax would be determined at the date of disposal, the deferment of the winding up would H not have made any difference.

Learned counsel for the respondent here submitted that the relevant special resolution passed was before the tax advice. There was an attempt made to pass a second resolution at an extraordinary general meeting on 15 January 1993 to defer the winding up and the notice was dated I 17 December 1992. However, the petitioners' application for an injunction came up before the meeting date. The injunction was never heard on the merits because of procedural matters but the respondent gave an

A undertaking not to proceed with the meeting. As such, he added, the shareholders were never given an opportunity to reconsider the matter.

The first question, he asked, was whether the winding up court had the discretion not to order a winding up in the face of the resolution relying on *Byrom Motors (Pvt) Ltd v Dolphin House (Pvt) Ltd* [1958] 3 SALR 432 B which held that the court had a discretion in the matter and that s 259(1) of the Companies Act 47 of 1951, applied and that further, however, that the court should not withhold an order because of the possibility that the lesser might have been in a better position had the applicant followed a different method of liquidating itself.

The second question is whether the discretion was exercised judicially C as a section of the shareholders felt that they would be prejudiced by the additional tax. It was his view that the learned high court judge had not gone wrong In any aspect.

In *Lim Kar Bee v Duofortis Properties (M) Sdn Bhd* [1992] 2 MLJ 281, it was a case where a scheme was devised whereby the appellant, the D registered owner of some valuable land in Penang, agreed to sell the land to a company and also executed a trust deed declaring that he held the land in trust for the company. The said company was incorporated together with another company, Lim Kar Bee & Sons Sdn Bhd, the holding company, and were formed in pursuance of a scheme devised by a tax consultant to avoid payment of estate duty payable in regard to the said land if the E appellant/landowner died. In the original application before the High Court, the issues raised and contested were that the various documents prepared, though signed by the appellant, were not explained to him; that there was misrepresentation by his daughter and that there was also undue influence. In respect of these issues, the learned trial judge came to conclusions against the appellant and granted the order as prayed in the F originating summons. The appellant appealed and raised the question of illegality for the first time.

It was held by the Supreme Court that when the contract is not ex facie illegal, the court can still take judicial notice of illegality and refuse to enforce the contract even though illegality has not been pleaded but only in G the situation when facts which have not been pleaded emerge in evidence in the course of the trial showing clearly the illegality. They also held that the real test to be applied in any given transaction seems to be whether the primary purpose of the transaction is to avoid tax; if it is, it is an illegal purpose, that is, of such a nature that, if permitted, it would defeat the tax law in question, coming under s 24(b) of the Contracts Act 1950. Since, H from the facts, the primary purpose of the scheme in that case was to avoid paying estate duty, especially bearing in mind that the said land would practically remain with members of the immediate family of the appellant/ landowner in the sense that the children and the wife of the appellant/ landowner would control exclusively the holding company without their having paid one cent towards the purchase price of the said land, the I Supreme Court was of the view that the scheme was therefore illegal and the agreement of sales and purchase of the said land and the subsequent trust deed were therefore unenforceable.

It cannot be disputed that it was the intention of the shareholders to defer the winding up to minimize the payment of income tax, and this clearly is an illegality, not realizing that as the tax would be determined at the date of disposal, it really would not have made any difference as to when the winding up takes place.

Having considered the arguments and the authorities, we were of the unanimous view that the learned trial judge was in error when he refused to order the winding up. Accordingly, we allowed the appeal with costs here and below, refunded the deposit to the appellant and granted the order in terms of the winding up petition.

Appeal allowed.

Reported by Jafisah Jaafar